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EC Calls Spain,s Budget Trends Unsustainable

1.(U) A European Commission study says the GOS needs to make serious budgetary adjustments to assure long-term sustainability. Over the past three years, Spain,s sustainability indicator (S2), which measures the impact of debt and spending, has grown from 3% of GDP to around 12%, nearly twice the EU average. Without significant budgetary modifications, the study estimates that Spain,s public debt, now not far over 50% of GDP, will grow to 528% of GDP by 2050. The EC recommends increasing revenues, cutting spending, and reforming the public pension and health systems. (El Pais, 10/15)

Prices Fell 0.2% in September

2.(U) The National Statistics Institute confirmed that consumer prices fell 0.2% in September after rising 0.3% in August. Prices in September were 1.0% below their level of September 2008. Underlying inflation (not including energy or food prices, which are more volatile) dropped to a year-on-year rate of 0.1%. (National Statistics Institute, 10/13)

Moody's Warns Banks are Understating Losses

3.(U) Spanish banks are risking future growth by not recognizing the full extent of their losses, according to a report issued this week by Moody's. Restructuring loans and accepting property in exchange for unpaid mortgages are keeping defaults off the books. Moody's warns that failure to address the situation more directly could hamper recovery from the economic crisis. Rigorous banking regulations, requiring significant reserves, have provided a good buffer thus far. However, given the continued economic downturn, Moody's says current reserves would cover less than half of an estimated 108 billion euros in losses. Should the economy continue to deteriorate, losses could reach up to 225 billion

euros. The president of the Spanish Banking Association (AEB) denied that banks are hiding losses and countered that they are weathering the crisis well, pointing to 8 billion euros in earnings during the first quarter of 2009. Comment: The AEB does not represent savings banks ("cajas"), only traditional banks. (WSJ, 10/13; El Pais, 10/14 and 10/16).

International Firms Playing Role in Caja Restructuring

4.(U) Morgan Stanley, KPMG, and UBS are among those playing a role in restructuring Spain's financial sector. Savings banks ("cajas") have been the financial institutions hardest hit during the economic crisis, due to their heavy exposure to the construction and real estate sectors. The Bank of Spain has called for consolidation of cajas (there are currently over 40, many small) to make them stronger and more competitive. Last June, the GOS created the Fund for Orderly Bank Restructuring (FROB), which will be able to leverage up to 90 billion euros to facilitate mergers and other restructuring. Now several significant mergers are in the works. Morgan Stanley is advising three cajas in the Catalan region -- Caixa Manresa, Caixa Catalunya and Caixa Tarragona -- whose merger would create the fourth largest savings bank in Spain. They are seeking around 1.5 billion euros from the FROB to effect the merger. KPMG is assisting Caja Espana, Caja Duero and Caja Burgos, while UBS has been working with Caja Castilla La Mancha, which authorities took over in March. (El Pais, 10/14; El Confidencial, 10/16)

Job Cuts Key as Opel Talks Continue

5.(U) National and regional government officials, including
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Industry, Tourism, and Commerce Minister Sebastian, met with union leaders and Magna representatives during the week to discuss the plans of the Canadian-Austrian firm Magna for Opel's Figueruelas plant once Magna completes its proposed purchase of a controlling stake in Opel from GM. Magna's current plans reportedly call for cuts of at least 1,350 jobs from the Figueruelas plant, which currently employs 7,500. These cuts would also lead to the loss of thousands of jobs by local suppliers of the plant. Spanish labor representatives have urged the government to impede signing if it will mean significant job losses. One article says union representatives are unwilling to accept cuts of more than 1,000 jobs. Magna plans to divert some of the plant's production to Germany's Eisenach plant but has committed to keep 70% of the plant's production at Figueruelas, to increase to 72% in 2013. Discussions continue, and a deal is expected to be signed in the next few days. (Multiple media, 10/16; El Pais, 10/15; El Mundo, 10/15)

Renault to invest 500 million euros in Valladolid facility

6.(U) Renault Spain has announced plans to invest 500 million Euros in its Valladolid facilities, guaranteeing the plant's livelihood for the next ten years. Renault plans to build an electric car there starting in 2011 and a new "ecological engine" vehicle in 2012; the electric car would be the first to be mass-produced in Spain. President Zapatero says this is proof that the Spanish industry remains competitive despite the automotive slump resulting from the economic crisis. Renault currently employs 5,000 workers directly at the Valladolid facility and is indirectly responsible for another 30,000 jobs in the region. (WSJ, 10/6; El Pais, 10/7)

CNC Opens Sanctions Proceedings Against Electric Companies

7.(U) Spain's National Competition Commission (CNC) announced it will begin sanctioning proceedings against nine major electricity companies, including Iberdrola, Endesa, and Gas Natural. The CNC says it found sufficient evidence of anti-competitive practices among the companies during a preliminary investigation. Specifically, the CNC contends that between 2004 and 2008, these companies withheld

electricity from the market in order to inflate prices, supported by actions by their distribution operations. The decision to open the proceedings demonstrates the CNC's resolve to address anti-competitive practices as the electricity market continues the liberalization process initiated in 1998. (Expansion, 10/5; ABC, 10/6)
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